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2008 BUDGET SUBMITTED TO PARLIAMENT ON 9/25/07

¶1. (U) The government proposes to spend Euros 289.8 billion and collect Euros 301.6 billion in taxes, which represents a projected budget surplus of 1.15% of GDP. The budget surplus assumes Spain will grow by 3.3% in 2008, which is still a reasonable, albeit somewhat optimistic, forecast given the international financial market turbulence and Spain's construction slowdown. The opposition conservative PP party has criticized the budget as not being stringent enough, although it has not offered proposals leading to an overall higher projected budget surplus. The "political" nature of the budget (elections are expected in March 2008) is apparent in that social spending will go up, especially for disabled people and to help lower-income and/or young people afford housing. The government is also emphasizing social spending more in its media strategy.

¶2. (U) Infrastructure investments in the autonomous communities (the equivalent of American states) is slated to go up by 14.4%. The PP says the distribution of spending is politically skewed because investment in Catalonia (a crucial electoral battleground - if usually PSOE voters abstain, the government could easily lose the elections) is slated to go up by 22.6%; in Andalucia (a PSOE stronghold) by 20.9% and in the Balearic Islands (which now has a Socialist president) by 24.3%. Infrastructure spending in the Madrid region, a virtually impregnable PP fortress, will see spending go up by only 0.1%. The government defends itself, however, noting that infrastructure spending in Valencia (another PP bastion) will go up by 25%. In fact, Valencia will see the highest increase, largely because of the high-speed train being built between Madrid and Valencia.

¶3. (U) Spending on R&D, a government priority, is slated to be Euros 7.7 billion, which is a 164% increase from when the

government took office in 2004. Defense spending is projected to rise 5.9% to euros 8.1 billion, still a little less than 1% of GDP, although arguably R&D spending in other ministries pushes the amount for defense to over one percent of GDP. Although the government will finance many infrastructure projects by acquiring debt, the national debt as a percentage of GDP is projected to be 34% of GDP in 2008, down from 37.7% in 2007. The budget still needs to be approved by parliament, but presumably the government has already gotten pledges of support from the smaller parties to obtain passage of the budget. (El Pais, 9/26/07)

¶4. (U) Comment: Given the current uncertainties in the financial markets, most economists would prefer a more restrictive fiscal stance. However, the Spanish fiscal picture needs to be seen in the context of the fact that Spain is the only big EU economy projected to run a budget surplus in 2008. Moreover, public debt as a percentage of GDP has declined from 46.4% of GDP in 2004 to a projected 34% in 2008. Having said that, 2008 is shaping up to be a year of uncertainty. During the last three years, Second Vice President and Finance Minister Pedro Solbes has released forecasts that wound up on the low side of actual growth. He will be hard pressed to repeat this in 2008. End Comment.

OECD'S "EU ECONOMIC PANORAMA" REPORT LOWRANKS SPAIN

¶5. (U) Within the Euro zone, only Portugal is further behind the U.S. than Spain in terms of GDP per capita. The same is true with respect to productivity. Spain also has a high regulatory burden, and a relatively low percentage of the labor force has university training. University of Chicago and London School of Economics Professor Luis Garicano is quoted as saying that Spain's economic model has permitted it to get to the "first division" but "not to remain in it." (Expansion, 9/21/07)

ENVIRONMENT MINISTER NARBONA ARGUES FOR PASSAGE OF

BIODIVERSITY LAW

¶6. (U) The new law would enshrine the "precautionary principle," which has been used by the EU to prevent, among other things, agricultural biotechnology approvals and to impose draconian coexistence laws in the agricultural field. The opposition conservative PP party criticizes the new law as too "interventionist." (Comment: Despite Minister Narbona's well-known opposition to agricultural biotechnology, recently the government has been less restrictive.) (Expansion, 9/25/07)

EVEN IN WEALTHY MADRID, 48% OF WORKERS GROSS LESS THAN A THOUSAND EUROS A MONTH

¶7. (U) Although National Statistics Institute information indicates that Madrid workers' average monthly salaries of 1,908 euros makes Madrid the country's highest-earning Autonomous Community, this average includes many lower-paid workers. According to a study by the Workers Commission labor body, one in five Madrid workers struggles to survive on less than 600 Euros a month. The Commission says the data shows a growing disparity between stable employment and precarious or temporary employment. One out of 5 Madrid workers makes less than 513 euros a month, and 13% must conform with 256 euros. Many of the lower-paid are in construction or hotel services, while many of the 13% who gross more than 2,565 euros a month work in the finance sector. (20 Minutos)

TELEFONICA EXPANDS COVERAGE IN BRAZIL/LATIN AMERICA

¶8. (U) Mobile telephone operator Vivo, controlled by Telefonica and Portugal's Telecom, will soon have nation-wide mobile coverage in Brazil after winning a tender to expand its already existing coverage to six Brazilian northeastern

states. Vivo, the leading mobile telecommunications operator in Latin America, currently enjoys 28.4 percent of the Brazilian mobile telecommunications market. The Telefonica group manages one-third of all Latin American telecommunications business, including fixed lines and mobile telecommunications. It is the largest foreign investor in Latin America of any industry and has a particularly strong presence in Brazil, Argentina, Chile, Peru and Colombia.

CORRUPTION AND COASTAL DEVELOPMENT IN SPAIN'S MALAGA PROVINCE

¶9. (U) Documents from the prosecutor's office in the province of Malaga reveal that in 2006 the prosecutor's office processed more than 243 reports of abuses related to urban growth and potential corruption. These and other cases relating to illegal construction projects have resulted in judicial action against 20 out of 100 mayors in the province of Malaga. Given the burgeoning profitability of the construction sector over the past several years, many coastal municipalities have turned a blind eye to construction projects in areas that are not zoned for such purposes. Construction efforts as well as the tourism that is related to this industry have been a significant money maker for municipalities which otherwise do not receive large amounts of funding from the central or provincial governments. In addition to uncontrolled urban growth, this illegal construction activity at its worst has been linked to money laundering schemes, bribery, and falsification of documents on the part of municipal officials.

ABENGOA TEMPORARILY CLOSES ETHANOL PLANT DUE TO HIGH COST OF WHEAT AND BARLEY

¶10. (U) Abengoa announced this week the temporary closure (second time this year) of one of its Spanish ethanol production plants, apparently due to high feed stock (wheat and barley) prices and lack of domestic demand for ethanol in transport fuels. The plant, Babilafuente, a joint venture with Ebro Puleva, has the yearly capacity to process about 600,000 tons of feed stock in the production of about 200 million liters of ethanol. Abengoa closed the plant last May for the same economic difficulties cited in this closure, but reopened in July during the domestic wheat and barley harvest.

¶11. (U) The plant owners had intended to sell the local ethanol production into the Spanish market, but cannot do so because of its limited current acceptance in the domestic market. This is due partly to the fact that the Government of Spain delayed the start of mandatory ethanol mixing from 2007 until 2009. As a result, Abengoa has been forced to sell locally produced ethanol to other European markets, adding to logistical costs and increasing operating losses.

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